

A Strategy for Jobs In the Inner City



The Enterprise Jobs Zone



A New Idea for "Greenlining"

Urban America

by Rep. Jack Kemp

Most people, when they think of it at all, associate inner city decay with the Northeast—the loser in some national war of demographics. The problem actually touches almost every part of our nation, and all of our people. It is rare today to find a major American city without an area totally deteriorated, lacking in industry, services, and population. Particularly in our older cities, these areas cover the heart of a city and symbolize the decline of an entire region. Middle and upper income residents have moved out, and small footloose industries—the key to new growth and new jobs—have gone to the outer fringes of the suburbs or to small towns.

Because the Northeast is so heavily urbanized, this mass exodus hits it hardest, producing chronically high unemployment, sluggish economic growth, a declining tax base and rising tax rates, and an inordinately high cost of living. Between 1970 and 1979 population in the Northeast actually declined, even though U.S. population grew 8.3 percent. Between 1970 and 1974 northeastern metropolitan areas experienced a net migration and a net job loss. A walk through the South Bronx, certain parts of Buffalo, and many other American inner cities is testament that inner city decay is no less brutal today than it was in the 1960s. Indeed, to those who continue to suffer it is even more tragic.

We are told that Washington's "best and brightest" have already attacked the problem. Since the 1960s government has produced an array of imaginative programs for the inner city. But while some achieved acceptable results, many of these programs became part of the problem. Who can forget Urban Renewal, which bulldozed gaping holes in our urban areas? What about "model cities" and "new towns" (now ghost towns)—programs which achieved remarkably forgettable results?

The fact is, while social welfare spending has increased every year (nearly one-quarter of the non-defense budget was spent in the central cities in FY 1979) inner city poverty remains intractable. We may keep the poor from starving, but we have failed to deal with the root causes of inner city poverty, to meet the needs of people groping for help and a chance to make it on their own.

Today a segment of our population is trapped in a cycle—a poverty trap—which has no beginning and no end. Without government help, some 43 million Americans—20 percent of the population—would be classified as poor. Why has this percentage remained the same for the past dozen years, despite creation of millions of new jobs and rising nominal wages? That is the paradox of our inner city decline.

I sometimes get the feeling that just because people are poor, policymakers think they are economically illiterate. Our inner city poor may, in fact, understand more about economic disincentives and price theory than many of our most learned members of the Council of Economic Advisors. A person today who gives up welfare or unemployment benefits to take a job that provides scarcely more, if any, in after-tax income than those benefits provide is just not being realistic. But that is exactly what we ask of our inner city poor. Government has spent in the past decade upwards of \$150 million to study people on welfare. But what

motivates—or doesn't motivate—welfare recipients in their economic decisions? That's something our welfare experts haven't figured out. I would make the case that the poor are motivated by exactly the same things as all other people: incentives, rewards, jobs that bring dignity not despair.

In 1975 Nathan Glazer of Harvard University described a case reported in the *Boston Globe* in which a family on welfare had "cash income and free health and educational services" amounting to \$16,028 a year, and no welfare fraud was involved. Glazer noted that, "A working head of family would have to earn at least \$20,000 to match this standard of living."

While this is an extreme example, a more common case is the person receiving the equivalent of \$8,000 a year in welfare benefits who is offered a job earning \$8,000 a year. He or she works for nothing if taking the job entails losing all the welfare payments. *The person faces a tax rate on work of 100 percent* (it would actually be higher because the person earning \$8,000 would have to pay taxes). If the person took a job paying \$10,000 in take-home pay, the tax rate would be an astounding 80 percent. Yet we seem surprised that many welfare recipients are often reluctant to take jobs. As writer Tom Bethell, a noted commentator on the subject, has pointed out: "Not even millionaires encounter tax rates that high."

If you want to work your way up the ladder of opportunity and success in America, you must first be able to get on the ladder. But with this system, the inner city poor are denied access even to the bottom rungs by the poverty barrier of high welfare tax rates on work and the high rates of inner city unemployment.

In other words, what government gives them with its right hand, it takes with its left. We offer the poor transfer payments, then tax their earnings so brutally they have little choice but to accept them. We give grants and loans to businesses that are paid for by increased taxes which endanger the very enterprises most likely to offer new opportunities to the disadvantaged. We provide training for jobs which, because government has created a business environment hostile to small-scale entrepreneurship, are never created.

Then we act surprised when our inner city residents become so discouraged they remain permanent fixtures on the public dole. Vernon Jordan, President of the Urban League, calls them America's "boat people without boats, cut adrift" from the promise of a better future. Is it any wonder they are becoming poorer, more despairing, and more dependent?

Entrepreneurial Calculations

This does not mean the situation is hopeless. When it comes to his or her own personal welfare, every individual is an entrepreneur. Everyone makes economic calculations. Our inner city residents who stay on relatively high-paying welfare instead of taking tax-paying jobs make an economic calculation. What we need is a fair program that

encourages a change in that calculation. People want to work, want to save, want to be productive. Our economic policies just aren't giving them that chance. But that's only the first of two aspects of our urban problem.

The second aspect is that skilled workers and experienced entrepreneurs are leaving the inner city for the suburbs and beyond. When the skilled and established entrepreneurs leave, leaving behind potential inner city entrepreneurs who are discouraged from taking risks, innovation and enterprise dry up. These skilled individuals make calculations too. So we need a national strategy which can help change their calculations.

Professor Peter Hall, a distinguished British specialist in urban affairs, describes this situation: "Some entrepreneurs (in the city) succeeded and grew large. As they did, they (often) took their business out of the city in search of larger scale, rationalized production processes. Others stagnated or even died; but there were always others to take their place, and again some of those would succeed. Now we have succeeded in killing off an abnormal proportion, and too little innovation is happening to fill the gap." The job is to discover how to get the innovation going again.

Our cities have traditionally been the seedbed for this innovation, its main engine of growth and jobs. Even today studies by the Massachusetts Institute of Technology and the Commerce Department show an important way of restoring new life to the inner city is to encourage new, small, technically-based companies to start up in the cities (today similar firms line small industrial parks in the suburbs). These companies would offer new employment opportunities to inner city workers, as well as a base for revitalizing retail and service industries.

To me these two problems—the flight of entrepreneurs and the disincentives facing those left behind—suggest the need for a new approach to our cities. While there are no perfect solutions or easy answers, we know that we can't continue promoting more of the same.

When the inner city is in trouble, the traditional response is to pump more aid and more programs through Congress. In 1978 President Carter said: "I am convinced that it is in our national interest to save our cities. I intend to provide the leadership." But only a few months following his announcement of a new national urban policy, Mr. Carter's grandiose promise to rebuild the South Bronx "brick by brick and block by block" was exposed as tokenism. It's easy to understand why. The Administration was offering just more of the same. More bureaucracy for the inner city resident, more programs that had already failed, more disincentives for the individual.

We don't need more of the same. What we need is a program based on an understanding of what makes people—rich and poor—tick economically, and what motivates them in the marketplace.

If we clear away the federal underbrush surrounding our inner city, we recognize that the root cause of its decline is the lack of one element—economic growth. Our inner cities lack growth because they take the last place in innovation and economic risk-taking, and because

their residents face a system which frustrates human nature by weakening the link between effort and reward.

As the Chief Counsel of the Small Business Administration said recently, "The critical need is for an entrepreneurial environment far more favorable to innovation and risk-taking than we have had for the past ten years. . . . New concepts are only generated from individuals, and creative individuals need an environment that is conducive for creation with rewards, recognition, profits, freedoms, and the availability of capital, basic knowledge, and other tools with which to create. There appears to us to be a lack of understanding within government of how individuals create in the private sector, and how they implement their creations."

Notice we're talking not just about "capital formation" but about *capital mobilization*. Capital is not just money. If it were, then government could solve these problems by printing more of it, or we could double—triple—federal transfer payments to the poor. Capital, in my view, is productive capability and thus exists in the minds, hands, and creativity of the people—in the inner city and throughout the country. This capital has been deactivated by the effects of excessive taxation and regulation.

There are "experts" who view people below the poverty line as a national stigma, as though they suffered from a permanent affliction. They miss the point of how quickly such human "capital" can be mobilized in our inner cities. They miss how rapidly, in an entrepreneurial economy, the poor can move up the ladder of success, and the wealthy vice versa.

Enterprise Jobs Zones

Recently in *Harpers* magazine Tom Bethell wrote: "An economy is precisely kept in a dynamic state by two powerful forces: the push (from the bottom) of those escaping poverty, and the upward pull or magnetic attraction of wealth." This is precisely the rationale behind my legislative proposal—to restore incentives for that "push" and "pull." The essence of the legislation, The Urban Jobs and Enterprise Zone Act, is to classify the most decayed segments of our cities—and also very poor rural areas—as "Enterprise Jobs Zones." Congress would then attempt to "greenline" these areas by dramatically reducing tax rates in each zone for individuals and enterprises, to restore incentives for economic activity.

It is said categorically that government cannot provide tax incentives without losing a great amount of revenue. This is a mistaken principle. Government loses not a dime by dramatically lowering the tax rate on the unemployed black or Hispanic teenager. He or she is producing no taxable income for the government to lose. Neither does it lose by lowering small business tax rates in burned-out areas of the city. Almost all small enterprises have already left these areas. Unless Congress changes this situation with new policies, the Treasury loses potential revenue it could gain from a vibrant inner city economy.

Even assuming no revenue response to this proposal—that is, that individuals don't respond to incentives—the cost would still be relatively low. While a complete computer analysis has not yet been prepared, a rough, static estimate (with no feedback effects) is only \$1.4 billion. Assuming the standard Keynesian 30-percent revenue feedback effect, the cost would be \$1 billion. This is less than one-sixth the cost of community and regional development grants, less than one-seventh the cost of CETA, and less than *one-two-hundredth* the cost of income security transfer payments!

With this proposal, any unit of local government may apply for one or more Enterprise Jobs Zones within its jurisdiction, if (a) they meet eligibility requirements somewhat similar to criteria established by the Economic Development Administration of the Commerce Department for Special Impact Areas, and (b) the local government will agree to reduce its effective property tax rate within the Zone by five percent a year for four years.

The proposal's four major elements apply only within these Zones, and are targeted to smaller enterprises and individuals because 66 percent of new jobs created nationally, and 100 percent of net new jobs created in the Northeast, come from small business.

1) To encourage job creation in the inner city, particularly for the young, the bill reduces Social Security payroll taxes on employers and employees by 90 percent for workers under 21, 50 percent for workers 21 and older.

2) To encourage small enterprise investment and job creation, the bill reduces the capital gains tax rate on investment by 50 percent (on the sale of residential property, the tax reduction applies only when the seller has his or her principal residence in the Zone).

3) To encourage business expansion and to retain existing enterprises, the bill reduces business tax rates 15 percent across-the-board for any business located in and employing at least half of its employees in one or more Zones.

4) To increase small business incentives, the bill (a) allows three-year, straight-line depreciation on the first \$500,000 of assets purchased each year, (b) allows the use of cash rather than accrual accounting methods for firms with gross sales below \$1 million, and (c) extends the loss carryforward provision to ten years.

The Need for Noninflationary Growth

I am not saying that any bill alone will end urban blight. We also need a strong national economy, something increasingly distant in this time of nearly 20-percent inflation, rising tax rates, declining productivity, savings, and investment, and increasing joblessness. Our most pressing problem is the combination of this high inflation and our progressive tax system—a combination unprecedented in the history of our country, which is why for the first time in most of our lifetimes we are feeling our economic strength ebbing away.

Inflation—a decline in the value of money—by itself is destructive. High progressivity in tax rates by itself discourages labor and capital

from increasing their productive efforts. The combination of the two has been horrendous. Even as inflation saps our ability to save for the future, to invest in our futures, it lifts both labor and capital into high progressive tax brackets that smother the incentive to produce.

As we discuss ideas and strategies for revitalizing our inner cities, we should also consider repairing the damage done by a decade of inflation on our outdated tax code. This means reducing tax rates. I believe we need to reduce today's high personal income tax rates, to reduce and index capital gains and estate taxes, to adjust business depreciation for inflation, reduce the corporate tax rate, and reduce the regulatory load on business. We should also examine individual states' economic policies to see why they have produced varying economic conditions within the same region.

While business incentives are necessary, wages and salaries alone account for roughly 80 percent of our national income. Thus the economic decisions of *individuals* command four times as much of production as the decisions of corporations. By restoring individual incentives—particularly in the inner city—we dip into our greatest potential source of increased production for economic growth.

Only by such measures can we solve the central problem of most of the inner city poor: the extraordinarily high tax rates they face when switching from welfare to jobs paying similar amounts in after-tax income. As long as government benefits are indexed to inflation while income taxes are not, this problem will persist. Until the rewards for work exceed the rewards for government-subsidized unemployment, it will further persist. The only humane way to increase these rewards sufficiently is to reduce tax rates.

President Kennedy, back in 1963, said in a message to Congress: "The most urgent task facing our nation at home today is to end the tragic waste of unemployment and unused resources, to step up the growth and vigor of our national economy, to increase job and investment opportunities, to improve our productivity, and thereby strengthen our nation's ability to meet its worldwide commitments for the defense and growth of freedom."

I don't remember him talking about enlarging a poverty class with more bureaucratic handouts and high tax rates. Nor did he talk about draconian cuts in the "safety net" of social services. He talked about reducing tax rates. He saw an America of boundless opportunity, where a man or woman anywhere could, with energy and initiative, reach as far or as high as he or she wanted. But when that initiative is stifled, as it is today, by a poverty wall and a tax system that denies individuals the incentive to "move up the ladder," people no longer exert themselves. When entrepreneurs find they cannot keep the reward for their efforts, they stop taking risks. Everyone reduces their economic effort, sometimes completely, and our country is thus deprived of the energy and spirit on which its greatness depends.

Our goal must be full employment for all Americans without inflation because nothing less is worthy of our nation and our nation's people.

THE KEMP-GARCIA URBAN JOBS AND ENTERPRISE ZONE ACT

'If you believe that what America needs is more people gainfully employed, more people producing goods and services, then you might be interested in the Urban Jobs and Enterprise Zone Act introduced by Rep. Jack Kemp.'

— William Raspberry, syndicated columnist.

'A bold, innovative approach like this is needed to restore the vigorous economic growth needed to create jobs for black Americans and other minorities.'

— Representative Augustus F. Hawkins,

Black Caucus member, and Chairman,
Subcommittee on Employment Opportunities,
House Committee on Education and Labor.

'We can't think of . . . a more attractive place to begin building a new political coalition for an effective federal government.'

— The Detroit News.

'The approach is neither conservative or liberal, but overwhelmingly pragmatic.'

— Michigan Representative Dave Stockman.

'The bill is an innovative approach to the problems of urban unemployment and economic decline, which have made the South Bronx look like Berlin in 1945.'

— New York Representative Robert Garcia.

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